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SUBJECT: NEW SOCIAL INSURANCE LAW: TEMPEST IN A TEA CUP,  
FOR NOW

¶1. (SBU) Summary. On September 24, Vladimir Meciar (HZDS) reached an agreement with Prime Minister Robert Fico (Smer) to support an amended social insurance proposal that will be submitted (and passed) by Parliament this fall. The final compromise will raise payroll taxes for upper-income earners and their employers, but overall changes will have much less impact on foreign investors than the original proposal from the Ministry of Labor and Social Affairs. Coalition partners were able to find common ground on social insurance reform, settling on an agreement that resembled HZDS' original proposal after Fico shifted responsibility for serious economic policymaking from the social democratic-leaning Ministry of Labor to the business-oriented Ministry of Finance. Media coverage of the social insurance debate was extensive, with journalists insinuating a serious split between HZDS and Smer. A significant split between parties may still happen in the near future, but not due to this issue or other substantive policy differences. End Summary.

#### New Law and its Effects

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¶2. (SBU) Slovakia's governing coalition approved a new social insurance program on September 24 to cover the large (over 1 billion USD) deficit in the public social insurance (pension) fund. The previous government partially privatized social insurance by allowing earners to invest half their social insurance payroll taxes in private accounts. This move proved popular with young professionals but led to a quickly growing deficit in the public social insurance fund. The two major provisions of the new legislation are:

- Income taxable for social insurance purposes rises from three to four times the average wage, the equivalent of a rise from 2,370 USD to 3,160 USD per month. Social insurance payroll taxes remain at 18 percent per year, the majority of which (14 percent) are paid by employers.
- Maximum contributions to private funds will be reduced from 50 to 33 percent for the next three years in order to increase solvency of the public fund. The 50 percent level will be gradually restored over the following three years.

The agreed upon proposal includes several modifications demanded by coalition partner Meciar, such as restoring the right of workers to simultaneously work and draw a pension. This draft also eliminated the original Ministry of Labor proposal to make all income taxable for social insurance purposes. With the full support of the governing coalition, the proposal will be introduced and passed unamended by Parliament in October and will take effect January 1, 2008.

¶3. (SBU) The final proposal raises costs for business by lifting the amount of income taxable for social insurance but should not significantly hinder the business environment over the long-term. US Steel, the largest American investor in Slovakia, estimates that the final proposal will cost them approximately 1.6 million USD next year. US Steel had

estimated, however, that the original proposal to make all income taxable would have cost them over 4 million USD in 2008. The American Chamber of Commerce was very active in its opposition to the original proposal, and it appears that AmCham communication with Prime Minister Fico and business-friendly elements within Smer influenced the revising of the Ministry of Labor's original proposal.

HZDS and Smer

14. (SBU) Ironically, after months of public fanfare, the final social insurance proposal approved by the governing coalition closely mirrors the original social insurance quietly drafted at the Ministry of Labor by HZDS State Secretary (Deputy Minister) Peter Sika. Sika explained to

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Poloff the rough outline of this proposal in April. Sika's proposal never saw the light of day (or media coverage), however, since Minister of Labor Viera Tomanova (Smer) ordered significant changes based on suggestions from Ivan Bernatek, the Smer-appointed director of the social insurance fund. Over the course of the summer, Tomanova's position weakened due to scandals involving social insurance taxes owed by the NGO where she was working when she was appointed to her current position. The scandal led to the growing general impression that Tomanova simply is not up to the job.

Fico thinks highly of Tomanova and does not want to show weakness in the face of the opposition. The Prime Minister used a fair share of his political capital to defend her, but his defense tellingly focused on the person rather than the policy.

15. (SBU) While maintaining social democratic rhetoric in public, by late August Fico had delegated authority to draft social insurance legislation to the pro-business Ministry of Finance. Based on the final proposal that emerged on

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September 24, and judging from conversations with relevant officials, it is clear that Smer and Fico were working closely with HZDS for several weeks. In a September 18 meeting with the DCM, Ministry of Finance State Secretary Peter Kazimir commented that his ministry was working on a "fourth pillar" proposal with increased caps and temporarily reduced contributions to private social insurance funds. The initiative issued by Meciar the following week featured the same content and phraseology. The coalition approved the complex proposal at its meeting within one hour.

Public Airing of Dirty Laundry

16. (SBU) Despite this behind-the-scenes cooperation, Meciar was still forced to flex his muscles publicly by asking the opposition for help -- according to one source, by walking into the opposition club and making his pitch. Meciar also pointedly reminded the Prime Minister, seated in Parliament, that he had also once been Prime Minister and was not to be trifled with. One source said that Smer parliamentarians openly talk of early elections as a way of getting rid of Meciar once and for all, with the possibility of a new coalition between SDKU and Smer. Comment: This seems unlikely in the short term but one thing Fico will not condone is being seen as anybody's puppet, particularly Meciar's. Tensions could come to a head again when Meciar reasserts his desire to have a deputy in the Slovak Information Service, which Fico has thus far denied. End Comment.

Media Spin

17. (SBU) Media coverage of the social insurance debate, which was extensive over the past two months, strongly suggested that Smer and HZDS were angrily disagreeing over policy to the extent that it could threaten the coalition. Journalists were quick to magnify tensions for three major reasons: 1)

most journalists dislike Fico and want to see conflict within the coalition; 2) Tomanova's bumbling style evokes socialist images for many and makes her an easy target; and 3) leading opposition figures such as ex-Prime Minister Mikulas Dzurinda (SDKU) actively suggested rancor within the coalition. (Although an SDKU MP very close to Dzurinda acknowledged to us that they knew Meciar and Fico would reach a compromise with little real trouble.) There are long-term tensions between the parties due to HZDS' inability to shape legislation at the ministerial level and its need to flash its veto card in coalition council in order to exert influence. Meciar did little to discourage media speculation that the coalition was bickering, since he sees it in his interest for HZDS to appear independent. Ultimately, however, media reports of a meaningful fracture within the coalition based on policy differences were greatly exaggerated -- but a possible fracture based on personality differences continues to loom on the horizon.

VALLEE